“Coming together is a beginning, keeping together is progress, working together is success.”

– Henry Ford, Engineer, Ford Motor Company
A message from the President

2005 proved to be another successful year for the Preferred Financial Group as we continued to build on the energy produced by our member companies. Together, we executed core strategies that resulted in solid financial results, increased sales, improved technology, enhanced service capabilities and expanded distribution. Nowhere is the energy of the organization more evident than in the engagement of our workforce, who will lead the Preferred Financial Group beyond its current horizons.

Financially, we surpassed all of our goals in 2005. The Preferred Financial Group had pre-tax earnings of more than $35 million, which generated an increase in its capital position to $982 million. Total assets grew by 8 percent to more than $1.8 billion, fueled by the continued growth of the annuity product line. Individually, Fort Dearborn Life realized strong earnings of $30 million while assets reached nearly $1.7 billion. Colorado Bankers Life saw a record profit of $42 million, increasing its capital to $16.2 million. Our strong capital position affords us the financial strength and flexibility necessary to reach our aggressive growth objectives and to finance continued business development.

A key component in the growth of the Preferred Financial Group continues to be expansion through mergers and acquisitions. I am pleased to welcome a new member company in Member Service Life Insurance Company as a result of the two organizations’ parent companies merging in 2005. Insuring more than 95,000 individuals, Member Service Life’s product portfolio includes group and voluntary worksite products sold predominately in Oklahoma and Texas. As a result of the addition of Member Service Life, we gained access to new markets and increased size and scale.

As we look to compete in an aggressive market and expand our service capabilities to meet the growing needs of the marketplace, we continue to make investments in technology, expand our management team and improve our processes. In 2005, Fort Dearborn Life introduced two new services for its clients with short-term disability insurance: Web reporting that provides claim activity online and telephonic claims intake. Colorado Bankers Life enhanced its producer experience by launching a new agent access system in which the agent can view policy information online. The companies continue to expand their technology to facilitate the delivery of information to customers and distribution partners in a more efficient and time-effective manner.

Responding to the market needs for new and enhanced products, Fort Dearborn Life introduced three new products in 2005. In conjunction with its sister company Dental Network of America, the company launched a new suite of dental products. The addition of PPO Basic and Voluntary PPO coverages complement the existing dental offerings and provide a comprehensive dental portfolio. Fort Dearborn Life also added new features to its long-term disability product to make it more competitive in the marketplace. Finally, to take advantage of a growing market segment, the company launched a Fixed Index Annuity series that gives policy owners the potential to earn more interest than they would in traditional fixed interest rate annuities but with the protection of a minimum guaranteed interest rate.

These new product offerings drove the Preferred Financial Group to achieve a strong level of organic growth in 2005. Increasing more than 60 percent, annuity sales reached $136 million - a strong finish given the challenging interest rate environment. Group benefit sales were also strong at $71 million, and Colorado Bankers Life achieved more than $111 million in sales, a 12 percent increase over 2004 and the third straight year of increased production. Overall, our premium income grew to $837 million, a 5 percent increase from 2004.

Throughout our evolution, we have demonstrated a commitment to our policyholders and partners by focusing on consumer needs while providing financial stability, professional service and innovative business solutions. We remain committed to managed growth, both organically and through mergers and acquisitions. I am excited about the future of the Preferred Financial Group as we continue to execute our growth strategies. I want to personally thank our dedicated team for the success of 2005, as our accomplishments would not be possible without the commitment of all of our employees, distribution partners, policyholders and insureds.

Best Regards,

Larry J. Newsom
President, Life & Subsidiary Operations
The expansion of technology and the increased expectation in quality of service demand that our business constantly adapt. New markets, mergers and acquisitions, product line enhancements and service deliveries continue to be pursued in order to expand our business and improve our operations in an efficient and cost-effective manner. The Preferred Financial Group has strategically prepared for these opportunities, and it is our response that determines the success of our organization. During a time of considerable market change and consolidation, our energy has been focused on constant improvement.

**Our Companies**

As subsidiaries of Health Care Service Corporation (HCSC), a Mutual Legal Reserve Company, Fort Dearborn Life Insurance Company, Colorado Bankers Life Insurance Company and Member Service Life Insurance Company operate within an organization that insures more than 10 million members. Our relationship is reinforced with the resources shared between companies, including affiliates Combined Services LLC and Dental Network of America, Inc.

All three members of the Preferred Financial Group received improved financial ratings from A.M. Best Company in 2005. Fort Dearborn Life’s impressive upgrade to an “A+” (Superior) rating is significant as it brings the company into an elite group of commercial carriers with “A+” (Superior) or better ratings. Colorado Bankers Life and Member Service Life were both upgraded to an “A” (Excellent) rating, reinforcing each company’s commitment to financial stability and operating efficiency. These notable financial ratings reflect the strategic value of Fort Dearborn Life, Colorado Bankers Life and Member Service Life to their parent company and recognize the strength of their businesses.

Fort Dearborn Life continues to offer valuable insurance benefits to meet the needs of employers and employees, as well as an attractive line of fixed and index annuity products for individuals planning for retirement. The company has continuously demonstrated a commitment to its strategic partners by focusing on customers while providing professional service and innovative business solutions. Building on integrity and honesty, Fort Dearborn Life’s goal is to develop and reinforce lasting relationships with its customers that span not only years, but decades.

Colorado Bankers Life provides affordable employee-funded voluntary insurance benefit programs and individual family financial plans. With a unique understanding of the costs and complexities associated with employee-funded benefit programs, the company succeeds in simplifying the process for both the employer and the employee through administrative operations and technology unique to its markets and distribution.

In conjunction with the 2005 merger of HCSC and Blue Cross and Blue Shield of Oklahoma, Member Service Life joined the Preferred Financial Group. Based in Oklahoma, Member Service Life offers life and disability plans with a respected, trusted reputation for protecting a family’s financial security in the event of unforeseen death and disability.

Combined Services LLC specializes in providing customized solutions for companies and individuals, enhancing our already strong product lines. Marketing primarily in the New England area, Combined Services LLC distributes a comprehensive array of group and worksite insurance products.
Fort Dearborn Life's Group Benefits division created the FOCUS on Small Business program that is designed to equip small business owners with employee benefit packages comparable to that of large corporations. The program features a comprehensive portfolio of group life, short-term disability (STD) and long-term disability (LTD) insurance plans designed specifically for the small business employer with two to nine employees. The broad range of group benefits offered is affordable, easy to implement and simple to administer.

To provide employers and their employees with more affordable access to dental care, Fort Dearborn Life launched its first national preferred provider organization (PPO) group dental insurance program. This expansion of basic and voluntary dental products allows the company to better meet the needs of its customers by offering more choices.

Fort Dearborn Life's expanded LTD contract solidified its position in the competitive disability marketplace. The new contract strengthens plan design and increases pricing flexibility while strategically aligning Fort Dearborn Life with large disability carriers. Released with this enhanced LTD contract was a unified proposal that covers all life, STD and LTD insurance products, streamlining the application process for employers.

In conjunction with Member Service Life, Fort Dearborn Life introduced a new product for its customers in Texas. Occupational accident insurance is designed for companies and their employees that choose to be nonsubscribers to the Texas Workers Compensation System. This product provides benefits in the form of medical, death and dismemberment and disability payments to employees who suffer workplace accidents.

To provide cost-effective solutions for individuals who want limited benefits for spouses or children, Colorado Bankers Life introduced a family rider for its critical illness policy. Building on the success of its individual critical illness coverage, Colorado Bankers Life also received regulatory approval for a group critical illness policy. These products provide living benefits to individuals diagnosed with a critical illness regardless of treatment, actual expense or other coverage.

Markets

Fort Dearborn Life remains committed to its relationships with Blue Cross and Blue Shield partners throughout the country. During 2005, we widened our distribution in the Northeast with the addition of Blue Cross and Blue Shield of Vermont. We are focused on maintaining mutually beneficial partnerships while proactively engaging new partners to join our distribution network.
A strong dedication to small business enabled Fort Dearborn Life to enter the Michigan small group marketplace as the exclusive provider of ancillary group benefits for the Small Business Association of Michigan (SBAM). While the relationship will provide SBAM members with comprehensive and affordable group life and disability products designed specifically for small businesses, the partnership will also allow Fort Dearborn Life to participate in the small business market on a national level.

Fort Dearborn Life’s group business continues to benefit from its broker direct strategy, generating positive results across the United States. By staffing offices with sales professionals and account executives who have established relationships within their communities, the company effectively ensures a place in the local group market. This strategy has allowed further expansion into a larger geographical area.

This successful strategy culminated with the recent openings of Fort Dearborn Life sales offices in Atlanta, Indianapolis and Nashville, where performance in the first calendar year of production well exceeded 2005 goals. We anticipate continued success with the company’s newest sales office in Denver, which opened in the fourth quarter of 2005.

Building on the broker direct strategy, Combined Services LLC increased its producer distribution network with the addition of a sales office in Connecticut. The timing of this sales office complemented Fort Dearborn Life’s approval of basic and voluntary PPO dental products in that state. Connecticut producers can now access Fort Dearborn Life through Combined Services LLC for all of their group and voluntary life, disability and dental needs.

Improving the geographic reach of our annuity distribution was a key initiative in 2005. Historically concentrated in the Northeast and Midwest, Fort Dearborn Life successfully partnered with a select number of independent marketing organizations with experienced producers in order to realize its objective. These partners understand and consistently promote the power of Fort Dearborn Life’s brand, enabling the company to effectively grow its asset base.

The addition of Member Service Life allowed Fort Dearborn Life to expand even further. As a company whose product portfolio includes group life and disability products, as well as critical illness and occupational accident insurance, Member Service Life provides Fort Dearborn Life’s first opportunity to enter the Oklahoma marketplace.

**STRONG COMMITMENT**

We recognize the importance of a solid foundation for our companies to build upon. With our commitment to service quality, our ability to provide comprehensive marketing tools and our growing online capabilities, the operational framework of the Preferred Financial Group is stronger than ever.

**Strength in Numbers** In 2005, we embarked upon an ambitious plan to enhance key management positions throughout the organization. At the senior management level, Fort Dearborn Life hired four new vice presidents with extensive industry knowledge. Leah Bytheway joined the organization to lead Group Administration, and Linda K. Wagner was chosen midyear to head the Individual Life and Annuity division. Victoria E. Fimea joined as general counsel and secretary, and James Wiseman was named chief actuary shortly before 2005 came to a close. Additionally, Steven Klister assumed the role of president and chief executive officer of DNoA. This management team, along with the hard work and dedication of the existing staff, resulted in the realization of several key accomplishments and competitively positions the Preferred Financial Group for the opportunities that lie ahead.

**Communicating Our Message** To raise brand awareness, a fresh advertising campaign was launched by Fort Dearborn Life and implemented throughout 2005. Advertisements appeared in several nationally recognized trade publications, and larger presentation-sized ads were reproduced and displayed at sales offices across the country.

In addition to advertising, Fort Dearborn Life’s Group Benefits division introduced In Focus, a producer newsletter. Distributed quarterly, the publication is designed to keep the company’s partners informed of its latest news, as well as updates on products and services.
Growing Technology and Service Delivery

Nowhere is the Preferred Financial Group’s evolution more evident than in its investment in improved technology. Fort Dearborn Life’s public Web site was redesigned to provide an enhanced user experience, to reinforce brand identity and to prepare the site for future online service functionality. Features include “one-click” access to Producers Corner, Benefits Manager and Forms Download from anywhere in the site; additional sections dedicated specifically to employers and individuals; and an archive of company press releases. The revamped site also includes an extensive “Contact Us” section with superb e-mail functionality for customers, a site index, access to agent appointment information and a group benefits sales office locator.

Fort Dearborn Life implemented two new capabilities for short-term disability insurance. To assist benefits administrators in servicing their employees, real-time pending and paid claim status reports were made available on the company’s Web site. In addition, employers now have another claim submission option with the introduction of an employer-focused telephonic claim intake service for short-term disability customers.

Piloted by Fort Dearborn Life’s Group Administrative Services division in 2005, an electronic policy and certificate delivery system expedites receipt of coverage certificates to clients. New customers are notified via e-mail when policy documents become available on the Benefits Manager portal of the Web site, ensuring timely and up-to-date information. This valuable service will be introduced on a national basis in 2006.

Colorado Bankers Life’s online access system allows agents to view policy information via its Web site. Since the company began utilizing this online capability, calls to its customer service center have declined by 6 percent, resulting in increased efficiency.

Combined Services LLC expanded its technological capability with a sales and commission accounting data system, as well as electronic scanning of all new and existing insurance business. As the company strengthens its administrative platforms to reach more customers in an electronic forum, it will deliver information to constituents in a more effective manner.

FUTURE GROWTH

Reflecting on the past year makes one thing clear: We can no longer use past success as an indicator of future performance. As we acknowledge the importance of planning and strive to provide superior value, we will continue to execute a comprehensive business plan that supports our growth.

Organization

Continued alignment and uniformity of functions, processes and systems will ensure consistent customer experience while leveraging the expertise of our three Fort Dearborn Life administrative locations and our Colorado Bankers Life Operations Center. 2006 will bring the consolidation of established call centers in Texas and Illinois as the company moves toward national customer support availability from 9 a.m. to 5 p.m. in all U.S. time zones.

Financial Management

Expense management continues to play a critical role in the Preferred Financial Group’s success. Over the years, we have demonstrated the ability to grow our business and implement technology while maintaining competitive expense levels. Our flexible operating model allows us to effectively manage our expenses as we expand our organization.

With the ability to integrate processes and functions in a turnkey manner, we will aggressively pursue acquisition opportunities in 2006. Given our strong capital, we are well-positioned to acquire and invest in businesses for both long-term strategic growth and short-term operational gains.
Responsiveness  Because we understand the importance of anticipating the actions of regulators and future laws, we proactively monitor regulatory and legislative bills and activities that may impact our insurance operations. Tracking bills that will eventually become laws enables us to remain abreast of and respond quickly to industry developments.

We are committed to the highest level of operational ethics. In 00, Fort Dearborn Life will institute a program to comply with the anti-money laundering regulations that were finalized in late 2005 as part of the USA Patriot Act.

Preparation  We will hone our product development process model to accelerate speed to the market. By staying connected to distribution partners who make the members of the Preferred Financial Group their companies of choice, we will follow a consistent and flexible approach to responding to market trends while quickly capitalizing on new opportunities. We are poised for action and will act boldly.

Technology  As part of the ongoing Web site redesigns for Fort Dearborn Life, new Benefits Manager, Group Producer and Annuity Producer portals are currently under development. Additionally, continuing system enhancements and upgrades will be key to maintaining our high level of corporate technical services.

Online member changes for list bill customers and electronic fund transfer for disability claim payments will be implemented, while online claim reporting capabilities will continue to be expanded. Fort Dearborn Life’s focus on system and process training is designed to ensure consistency of customer experience and improved quality and accuracy.

As Colorado Bankers Life works toward an electronic document management system, the company strives for a paperless environment by making insurance applications available via the Internet in 00.

Energized by innovation, expansion and growth, the Preferred Financial Group is positioned to exceed the expectations of an ever-changing industry.
**ASSETS (Dollars in Millions)**

- **Fort Dearborn Life**
  - 2006: $1,192.4
  - 2005: $1,360.0
  - 2004: $1,146.6
  - 2003: $1,710.3
  - 2002: $1,946.4

- **Colorado Bankers Life**
  - 2006: $1,681.4
  - 2005: $1,595.4
  - 2004: $1,478.9
  - 2003: $1,250.4
  - 2002: $1,044.4

- **Member Service Life**
  - 2006: $42.5
  - 2005: $39.8
  - 2004: $36.5
  - 2003: $34.3
  - 2002: $30.2

**CAPITAL/SURPLUS (Dollars in Millions)**

- **Fort Dearborn Life**
  - 2006: $28.9
  - 2005: $27.5
  - 2004: $25.1
  - 2003: $24.4
  - 2002: $23.0

- **Colorado Bankers Life**
  - 2006: $16.2
  - 2005: $14.0
  - 2004: $23.2
  - 2003: $21.5
  - 2002: $23.7

- **Member Service Life**
  - 2006: $122.5
  - 2005: $114.9
  - 2004: $117.7
  - 2003: $109.6
  - 2002: $106.0

*Does not include Member Service Life financials. **Reduction reflects redemption of $12 million of minority preferred stock, redeemed July 2004.*
Fort Dearborn Life
Colorado Bankers Life
Member Service Life
Preferred Financial Group

*Does not include Member Service Life financials.

REVENUES
(Dollars in Millions)

LIFE INSURANCE IN-FORCE
(Dollars in Billions)

$802.3
$791.6
$755.2
$727.6

$32.3
$30.5
$25.7
$23.3

$113,4
$111.1
$121.6
$126.0

$881.4
$835.5
$798.0
$769.4

*Does not include Member Service Life financials.
### Balance Sheet – Statutory Basis

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<thead>
<tr>
<th>Assets</th>
<th>2005</th>
<th>2004*</th>
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<tbody>
<tr>
<td>Bonds</td>
<td>$1,205,493</td>
<td>$1,153,413</td>
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<tr>
<td>Stocks, Policy Loans and Other Invested Assets</td>
<td>13,774</td>
<td>13,421</td>
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<tr>
<td>Cash and Short-term Investments</td>
<td>46,117</td>
<td>48,468</td>
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<td>Investment Income Due/Accrued</td>
<td>15,327</td>
<td>15,121</td>
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<td>Due and Uncollected Premium</td>
<td>34,216</td>
<td>32,218</td>
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<tr>
<td>Other Assets</td>
<td>13,219</td>
<td>16,221</td>
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<tr>
<td>Separate Accounts</td>
<td>518,235</td>
<td>431,413</td>
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<tr>
<td><strong>Total Assets</strong></td>
<td>$1,846,381</td>
<td>$1,710,275</td>
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</table>

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>2005</th>
<th>2004*</th>
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</thead>
<tbody>
<tr>
<td>Policy and Claim Reserves</td>
<td>$842,990</td>
<td>$848,688</td>
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<tr>
<td>Accounts Payable</td>
<td>60,046</td>
<td>57,857</td>
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<tr>
<td>Asset Valuation Reserve</td>
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<td>12,464</td>
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<td>Other Liabilities</td>
<td>25,846</td>
<td>16,429</td>
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<tr>
<td>Separate Accounts Liabilities</td>
<td>519,088</td>
<td>435,122</td>
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<tr>
<td><strong>Total Liabilities</strong></td>
<td>1,454,196</td>
<td>1,384,560</td>
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<td><strong>Total Capital/Surplus</strong></td>
<td>392,185</td>
<td>346,715</td>
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<tr>
<td><strong>Total Liabilities/Surplus</strong></td>
<td>$1,846,381</td>
<td>$1,710,275</td>
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</table>

(Dollars in Thousands)

*Does not include Member Service Life financials.

### Income Statement – Statutory Basis

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<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004*</th>
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</thead>
<tbody>
<tr>
<td><strong>Premiums</strong></td>
<td>$810,376</td>
<td>$765,333</td>
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<tr>
<td><strong>Investment Income</strong></td>
<td>66,165</td>
<td>65,310</td>
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<td><strong>Other Income</strong></td>
<td>4,836</td>
<td>4,870</td>
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<tr>
<td><strong>Total Revenues</strong></td>
<td>$881,377</td>
<td>$835,513</td>
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</table>

**Policy Benefits and Expenses**

| Benefits Incurred               | $673,544   | $668,208       |
| Commissions                     | 92,140     | 96,952         |
| Operating Expenses              | 68,692     | 57,044         |
| Insurance Taxes and Licenses    | 11,552     | 10,229         |
| **Total Benefits and Expenses** | $845,928   | $802,523       |

**Income**

| Gains Before Federal Income Taxes (Before Capital Losses) | $35,449 | $32,900 |
| Federal Income Taxes | 12,797 | 8,572 |
| **Realized Capital (Losses)** | 15 | (366) |
| **Net Income** | $22,667 | $24,049 |

(Dollars in Thousands)

*Does not include Member Service Life financials.